Commonly Asked Questions and Answers Relating to Individual Self-Iinsurance in the State of Kansas

Q. What do I do if my company wants to become self-insured?

A. If self-insurance is determined to be feasible by you and/or your insurance representative, write or telephone for a self-insured packet of information as indicated below:

Department of Labor
Division of Workers Compensation
Business and Accounting Section
800 SW Jackson Street, Suite 600
Topeka, KS 66612-1227
Telephone: (785) 296-3606

Upon receipt of the packet, either you or your Third Party Administrator should complete the following forms and file them at the above address:

1. Form 105, Application Oath to Become A Self-lnsured
2. Form 120, Application for Self-Insurance

The following should also be included in the mailing:

1. Five years of the most recent audited financial annual reports of either the parent company, or if none, the applicant company. In addition, file the most recent 10 Q or quarterly reports.
2. A copy of the safety manual and/or safety program.
3. Proposed excess insurance limits.
4. A copy of the Certificate of Good Standing from the office of the Secretary of State of Kansas

After a review is completed of the material submitted, we will contact you or your representative.

Q. My business has been in existence for four years. Is the business eligible for self-insurance?

A. A private firm must be in existence, doing business under its present corporate identity (continuous operation), for at least five years to make application; or is purchasing an existing self-insured Kansas firm, plant or facility and the operation of the purchased firm, plant or facility:

1. has been in continuous operation in Kansas for at least 10 years;
2. has generated an after-tax profit of at least $1,000,000 annually for the preceding three consecutive years; and,
3. has a ratio of debt to equity of not greater than 3.5 to 1. As used in this subsection, “debt” means the sum of long-term borrowing maturing in excess of one year plus the current portion of long-term borrowing plus short-term financial institution borrowing plus commercial paper borrowing, and “equity” means the sum of the book value of stock plus paid-in capital plus retained earnings. The method for calculating the amount of security required of self-insureds shall be reviewed by an actuary every five years, beginning in fiscal year 1997. The costs for these actuarial studies shall be paid from the workers compensation fee fund.

A corporation or other entity whose current identity is attributable to a merger or other transformation whereby the whole or a substantial part of a previous entity’s assets and income have been transferred to it, and its liabilities have not increased beyond the financial review requirements of the director, which qualified under its previous identity as a self-insurer under other provisions of the statute, and amendments thereto, may apply for renewal as a self-insurer under its new name. The director may grant the application for renewal if satisfied that the new entity meets all necessary financial criteria for renewal that would have been applied to the previous self-insured entity. An application under these provisions shall be limited to an entity seeking renewal based upon the prior self-insured status of another entity or entities.

A subsidiary corporation in business less than five years may be considered if its liability is guaranteed by a parent corporation. New applicants must submit five years of the ultimate parent's audited financial reports and the most recent quarterly statement or 10 Q.

Q. Are there state of Kansas statutes and regulations that pertain to individual self-insureds?

A. Yes. Refer to K.S.A. 44-532 and K.A.R. 51-14-4.

Q. How do I know if being self-insured is best for my company?

A. A self-insured employer is assuming the responsibilities provided by an insurance carrier; therefore, there must be a commitment on the part of top management to be self-insured, especially in the area of safety and loss control, claims review and payment to injured workers, and especially the setting and periodic review of reserves for future payment on known and existing claims. Also, an initial feasibility study should be made to determine if it is more cost efficient to be self-insured or to continue with an insurance policy.

For information purposes, the self-insured packet includes an exhibit showing the liability buildup of ten cases over a ten-year period.

Q. What are the financial requirements to be self-insured?

A. The self-insured employer or parent company should demonstrate financial strength and liquidity to assure all obligations will be properly met.

The Division of Workers Compensation performs a detailed review of the company's financial statements by reviewing the cash flow of the company. Other key ratios reviewed are liquidity, profitability and debt-to-equity. We then compare these ratios with other employers in the same type of business on a countrywide basis. Upon determining the applicable Standard Industrial Classification Code, a Dun & Bradstreet peer review is completed. The long-term debt of the employer is also monitored by Workers Compensation.

During this financial review, trending is performed to ascertain in what direction the employer is financially headed. The self-insured applicant is provided a copy of our financial worksheet printout.

Q. If a company has one or more subsidiaries they wish to be self-insured, are they combined on the same application?

A. If the subsidiary is **<u>separately incorporated</u>**, then each must have its own application. An Indemnity & Guaranty Agreement must be signed by the ultimate parent of the subsidiary guaranteeing payment of all workers compensation liability.

If the entity is a division not separately incorporated, then the two companies can be included on the same application.

Q. As a self-insured employer, are we required to have a Third Party Administrator assist us?

A. No. This is not a requirement, but an option. Many self-insureds have their own in-house staff of employees that do loss prevention services, handle their own claims, establish their own reserves and do other duties. If this is the situation, the employer must furnish us with the plan developed for adjusting claims. Item 6 of the Form 120, Application for Self-Insurance, addresses this issue, and Item 25 C requires the names, qualifications and experience of the person(s) evaluating loss reserves.

Q. If we retain a Third Party Administrator or an adjusting company, are they required to be licensed in the state of Kansas or domiciled in the state?

A. No. At the present time, the Kansas Insurance Department only licenses insurance agents. Third Party Administrators and insurance adjusters are not licensed. For self-insurance, we do not require Third Party Administrators to have an office within the state.

Q. What state of Kansas costs can I expect if our company becomes self-insured?

A. There are no premium taxes or administrative costs and, generally, no qualifying fees. There are two assessments to be paid annually: one to the Division of Workers Compensation and one to the Kansas Insurance Department, Workers' Compensation Fund.

The Division of Workers Compensation is a fee-funded agency, and assessment fees are assessed annually to finance the costs associated with the operation of the Division. No general fund monies are received. An information form describing the assessment procedure is included in the basic self-insurance packet.

The Kansas Insurance Department, Workers' Compensation Fund, annually assesses all self-insured employers an assessment to finance the second injury fund, and other responsibilities of the Fund.

Q. What are the assessments based on, who is assessed and what is the time table for making payments?

A. Every January, the Division sends a form to each self-insured, group self-insured (pool) and insurance carrier authorized to write workers' compensation insurance in the state, asking the amount of losses paid under law for the preceding calendar year. Based on that information, on approximately May 1 an assessment is levied against the losses paid and shall not exceed 3%. The assessment shall be paid prior to July 1 of each year.

The Kansas Insurance Department, Workers' Compensation Fund, uses the same claims paid-base during the preceding calendar year. Its assessment is due July 1st. Inquiries regarding the Kansas Workers' Compensation Fund should be addressed to:

Workers' Compensation Fund
Kansas Insurance Department
420 SW 9th Street
Topeka, KS 66612-1678
Telephone (785) 296-7062

Q. Is there an employee number or premium size requirement to be eligible to apply for self-insurance?

A. Yes. The self-insured applicant should have a minimum of 100 employees either entirely in the state of Kansas or on an interstate basis, i.e. 25 employees in the state of Kansas and 75 employees in the state of Missouri. This requirement is used to ascertain the size of the employer's operation.

Also, the self-insured applicant shall have a minimum manual workers' compensation premium of at least $250,000 - $300,000. A manual premium is the basic premium determined by multiplying the manual rate times each $100 of payroll per classification code. The referral to “standard premium” is the manual premium times the experience modification.

Q. How much equity should a self-insured applicant have to be self-insured?

A. Historically, self-insurance was an option generally for only the large and very large employers who could afford the exposure and expense of being self-insured. Otherwise, successive large losses might jeopardize the financial being of the company and cause it to declare bankruptcy. This would be especially true if the employer is highly leveraged, self-insured in numerous states and even self-insured in other lines of insurance such as general liability. Today, because of workers’ compensation market conditions and other factors, smaller employers are viewing self-insurance as a viable option to insuring their workers’ compensation exposure.

There is currently a $10,000,000 equity threshold and if an applicant has less equity, excess insurance, both specific and aggregate limits, are required. For applicants with $10,000,000-plus equity, specific limits are required but aggregate limits are optional.

Q. What is excess insurance?

A. Excess insurance is obtained from insurance companies in the same manner as obtaining primary insurance. A “self-insurance retention” amount is like a deductible amount on automobile or homeowners insurance, and for every accident or occurrence, the self-insurance retention must be paid by the self-insured. Once the self-insurance retention is paid, the insurance carrier is responsible. Generally, the larger and financially stronger self-insured employers have a higher retention and the smaller companies have a lower retention. Aggregate insurance is more costly to a self-insured employer, but is protected by placing a “cap” on the cumulative payments of claims. Once this aggregate annual cap, or “Minimum Loss Fund” is met, the self-insured pays no more and the insurance carrier pays up to the annual policy limit.

Q. What happens in the state of Kansas if the self-insured employer becomes bankrupt during the policy period and the bankruptcy freezes the funds of the employer? Are not typical excess policies written as reinsurance contracts and if the retention is met, the self-insured shall pay first and the excess insurance reimburse the self-insured employer?

A. Yes, you are correct. The standard excess insurance policy is similar to a reinsurance contract, but state of Kansas insurance laws protect the claimant. The state of Kansas excess insurance is viewed as “liability insurance” and if the self-insured employer cannot pay the claim, the insurance carrier must do so.

Q. Is an excess insurance policy required for all self-insureds?

A. Yes. Excess insurance is required for all self-insureds including public entities such as cities and counties. Excess insurance is often referred to as “catastrophic coverage” to provide protection for the large losses.

Q. Is excess insurance regulated by the Kansas Insurance Department?

A. Yes, because excess insurance policies are viewed as a “liability type” policy, each authorized insurance carrier with the authority to write workers compensation coverage must obtain prior approval of the excess policy form from the Kansas Insurance Department. However, the rates charged for excess workers compensation insurance are not approved by the Kansas Insurance Department, and there is no standard rate.

Q. How do I find an insurance carrier to provide an excess insurance policy?

A. The self-insured packet has a list of approved, admitted insurance carriers provided by the Kansas Insurance Department. The list indicates all admitted carriers who have had their excess insurance policies approved. The list also shows the companies authorized to write aggregate coverage. A commercial lines insurance agent will be able to provide assistance in locating an insurance carrier.

Q. I know of a non-admitted, surplus lines insurance carrier domiciled in Bermuda that can provide excess workers compensation coverage at less cost than a company on the list. Is this surplus lines coverage a viable option?

A. No. The state of Kansas insurance laws require insurance coverage to be placed with an admitted carrier even though the rates may be higher. However, the Kansas Insurance Department has a "white list" of surplus lines (not admitted) carriers that excess coverage can be placed with if insurance coverage is unavailable in the admitted market. If coverage is written by a company on the "white list," we require the policy to be filed with our office and amended to meet the requirements of what is required from an admitted company. Also, Form 133, Non-Admitted Insurance Carrier (Statement of Insured), must be completed and filed with us, and a written statement made by the self-insured administrator for forwarding to the Kansas Insurance Department by us reflecting the unavailability of excess workers compensation coverage in the admitted market. The filing of Form 133 and the written statement must be done at the time of each annual renewal of the excess policy.

Q. What happens procedurally after my self-insured company ceases to be self-insured?

A. After the termination date is determined and our office issues a letter of termination, we must be provided the name and policy number of the primary insurance carrier providing insurance coverage. The security posted will be required until such time there is no further claim activity, no open reserves and no known occupational disease exposure.

The security amount continues at the amount retained at the time of termination and is reduced by one-third until the end of the third year. If open reserves are present at the end of the third year, a factor of .25 is applied for Loss Adjustment Expense and future assessments if a Letter of Credit is used to post security, or a factor of .10 is applied if a surety bond is filed with us to the reserve amount, and an additional factor of .15 is applied for the cost of deficiencies in case loss reserves. These factors are applied annually.

Q. After the self-insured permit is terminated, how long will my company be assessed by the Department of Labor, Division of Workers Compensation and Kansas Insurance Department, Workers' Compensation Fund.

A. Your company will be assessed by our office and the Kansas Insurance Department, Workers' Compensation Fund, until a zero balance of paid claims during a calendar year period is reported.

Q. If my business is approved for self-insurance, how much security will I be required to post?

A. The amount of security that is required to be posted via a Letter of Credit or Surety Bond is determined after a thorough review of the financial stability and capability of the prospective company, and varies from one company to another.

Q. How is the security amount to be posted determined for new self-insured applicants and renewals?

A. The basic method used is our Security Determination Form developed in 1982, and updated during fiscal year 1997, by a consulting actuary. By statute, the form is now updated every five (5) years. The form has been very satisfactory in determining the amount to be posted. However, for large employers initially seeking self-insurance, it has appeared that the standard Security Determination Form would require too much security for the initial period. The consulting actuary provided an alternative method of determining the amount to be posted. The method used is to apply a .90 factor to the standard premium. The "standard premium" is the basic manual premium with the experience modification applied. The minimum amount of security is $350,000.

The .90 factor excludes insurance company profits, commissions, etc., but includes the pure premium, loss adjustment factor and related items pertaining to claims. At the time of renewal, we would then use our standard Security Determination Form as the self-insured's own reserves are determined. The pure premium of 60% ($.60 on the premium dollar) is that portion of the premium amount designated to pay losses. The Loss Adjustment Expense/Assessment Factor is 25% and is used to adjust and pay the claims, and to make allowance for future assessments.

For the small to medium size new applicants, we generally use the pure premium .60 factor as a reserve amount, and this appears to work well; therefore, the standard Security Determination Form can be used. For extremely small employers with a net worth of less that $10,000,000, aggregate insurance is required and the self-insured posts an amount equal to the Minimum Loss Fund, which is the point at which the insurance carrier begins paying all claims and the self-insured employer's liability ceases.

Q. What form must the security take?

A. The security amount may be posted by use of either a bank Letter of Credit or a Surety Bond.

Q. If I choose a Letter of Credit, may I use any bank?

A. You may select a bank of your choice; however, prior to the issuance of the Letter of Credit, the bank must complete a Bank Fact Sheet and submit a copy of the parent bank's, or if none, its most recent audited financial statement. After a thorough review of the bank, the Division will either accept or reject the bank as a Letter of Credit insurer. If rejected, another bank must be selected.

Q. What other requirements must be met for Letters of Credit?

A. Because the Division of Workers Compensation has no legislative authority to administer payment of claims, a Trust Operational Agreement must be established with a bank's trust department. The format for this agreement is available from the Division.

Q. Am I required to have the same bank issue both the Letter of Credit and the Trust Operational Agreement?

A. No, any bank willing to accept the state of Kansas wording for the Trust Operational Agreement is acceptable. The Letter of Credit must identify the bank where the Trust Operational Agreement is issued and located.

Q. Are there requirements the bank must meet to handle Letters of Credit?

A. The bank must complete a Bank Fact Sheet reflecting its financial condition as well as to provide a copy of their latest financial report for our review and acceptance. This review must be accomplished and approval granted prior to the Letter of Credit being issued. The Bank Fact Sheet and financial statement must be filed on the bank's ultimate parent bank, if applicable.

Q. What procedure is followed when a Letter of Credit or Surety Bond is called by the Director of Workers Compensation?

A. If it becomes evident that the self-insured is unable to pay the workers compensation claims as they become due, then the Director of the Division of Workers Compensation will call either all or part of the Letter of Credit or the Surety Bond. The funds are placed in the previously agreed to Trust Fund for the Letter of Credit, and the surety company pays in accordance with the terms of the surety bond. The funds are utilized to pay the claims as they become due.

Q. How long does it take to become self-insured?

A. After receipt of the completed application and the previous five years of audited financial records on the prospective self-insured company, permits have been issued in two weeks, but more realistically 30 to 45 days is normal.

Q. How long is the permit period in effect, and how often will I be required to renew the permit?

A. The permit normally is approved for one year or less initially, depending on when the fiscal year ends for the self-insured. Renewals are on an annual basis.

Q. What other options are there to cover workers compensation requirements if self-insurance is unavailable or not feasible?

A. Continue to purchase an insurance policy to cover the liability or join a pool of similar employers. Pool coverage (group self-insurance) is administered by the Kansas Insurance Department. Also, large deductibles are available now, and your insurance agent can assist you in this area.

Q. Are the self-insured records maintained by the Division and therefore the data provided by a self-insured company available to the public?

A. KSA 44-550b provides the following, quoted in part: "Records open to public inspection, exceptions. (a) All records provided to be maintained under K.S.A. 44-550 and amendments thereto shall be open to public inspection, except that records relating to financial information submitted by an employer to qualify as a self-insurer pursuant to K.S.A. 44-532 and amendments thereto."

Q. If the company wishing to become self-insured is a subsidiary of another corporation, whose financial statement is analyzed?

A. If there is a parent company, then the financial data and review is completed on the ultimate parent's financial reports, not the subsidiary. This is done because the parent has the ability to remove assets from the subsidiary at will.

Q. Does the state of Kansas require a meeting with the prospective self-insured company representatives prior to approval?

A. In order to hold down costs, there is no requirement for a meeting. Mailing of the two application (Form 105 and 120) forms and five years of audited financial reports will begin the process. Problems will be addressed as they arise with the appropriate representative.

Q. Assuming a qualified individual self-insured employer becomes bankrupt, cannot pay claims and the security is insufficient, do claims cease being paid?

A. No, the individual self-insured program has a "guaranty fund" to protect the injured workers. The law provides that the Workers' Compensation Fund (second injury), administered by the Kansas Insurance Department, pay claims of insolvent employers if other security is unavailable. The amount paid out is then assessed (post assessment) to all other self-insureds, group self-insureds and insurance carriers indicating paid workers compensation claims.

Q. Has a qualified individual self-insured ever declared bankruptcy, been unable to pay its own claims and the Workers' Compensation Fund had to make payments, and make an assessment for these payments?

A. No, not at this time.

Q. Is it a state requirement that the Self-insured Permit Certificate be posted or displayed?

A. No, this is optional and no permit certificate posting requirement exists. Regulation 51-13-1 does require all employers operating under the Workers Compensation Act to post a Form 40, Posting Notice, advising employees what to do in case of injury. The Posting Notice can be obtained by contacting the Topeka Workers Compensation office.

Q. A corporation is required to annually file documents and pay fees to the office of the Secretary of the State of Kansas to remain in good standing. How do I verify this to the Division of Workers Compensation?

A. Submit a copy of the certificate of Good Standing, which is issued by the office of the Secretary of the State of Kansas. This ensures that the corporation is approved to do business in the state for the current year. If not provided, the Self-Insurance application can not be processed.

Q. If I have additional questions or need further explanation, who should I contact?

A. Contact:

<u>Individual Self-Insureds</u>

Department of Labor
Division of Workers Compensation
Business Office & Self-Insurance
800 SW Jackson Street, Suite 600
Topeka, KS 66612-1227
Phone: (785) 296-3606

<u>Group Self-Insureds (Pools)</u>

Kansas Insurance Department
Commercial Multi-Perils Section
420 SW 9th Street
Topeka, KS 66612-1678
Phone: (785) 296-3071